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Economic Conditions
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General Business Conditions

THE business situation has shown little development during the past month, and the general feeling as the country enters the fourth calendar year of the depression is one of doubt and confusion. The state of trade indicates that economic relationships are still unbalanced, and that the disturbance in the terms upon which the various groups of the population have been accustomed to exchange their goods and services is persisting. Business men recognize the gravity of the problems and issues before the Government for action, and as long as their outcome is uncertain, capital is likely to continue timid and business to delay plans for expansion and replacement that would stimulate the heavy industries. The chief of all the causes of unsettlement and disturbance is the disorder in world trade and currency relationships, a situation which is the subject of discussion elsewhere in this Letter.

This is not a cheering state of affairs to face after three years of declining business and increasing unemployment, but there have been other depressions in which the outlook was as uncertain after as long a period, and they are matters of history now. The energies of the people and their productive capacity are not destroyed by the depression nor are their wants diminished. The difficulty is the breakdown in accustomed relationships, and during the three years readjustments necessary to restore practicable terms for trade have been going forward. Losses have been written off, debts discharged, and costs reduced. The situation shows that the readjustments have not been sufficient in all cases, but it cannot be contended that they have been without effect.

Deterioration Checked

It may be considered that in the past six months a ground for business recovery has been laid that had not existed hitherto in the depression. Taking the period in its entirety its outstanding characteristics have been these:

1. The contraction of credit has been halted, and the volume outstanding is larger at the end of the period than at the beginning. The financial situation has improved steadily since early Summer, and the growth of confidence in the country's money and in the general solvency of the banking system has relieved the pressure on credit and thus removed one of the causes of deflation. Funds have piled up in the centers, available to business when trade relationships are restored.

2. The decline in business activity has been stopped, and the level is higher at the end than at the beginning. The third quarter was a period of improvement and marked gains in activity, and the recession during the final quarter has been moderate in most particulars, not materially exceeding the seasonal expectation.

3. The decline in prices was stopped, and despite subsequent reactions, stocks and bonds hold well above bottom, while commodities are but little under the June low.

4. The piling up of commodity stocks has been checked. Although in the raw materials the improvement is not very substantial, stocks of manufactured goods in all lines are conspicuously low, and much below a year ago. The small stocks of automobiles in dealers' hands are an example.

This is the first half-year period since the beginning of the depression of which the foregoing could be said. Every other half-year has been one of deterioration in some or all of the factors cited.

Obviously it is of great importance that the deterioration of business in these respects has been stopped for as long a time as six months. This creates a basis of stability heretofore lacking, and the history of past severe depressions supports the idea that this is a necessary and usual precedent to improvement. It is worth remarking that the month of December, which in both 1930 and 1931 was a period of almost complete demoralization due to the efforts to establish losses and reduce inventories before the year-end, has been this year a month of stability in most markets. Moreover, such indexes of general business conditions as rail-

way car loadings and electric power production have shown during the month a smaller percentage of decline below 1931 than at any time since last Spring.

The question is sometimes asked whether there is any such thing as a minimum of replacement requirements upon which business activity may find bottom. The rebound since last Summer, and the mainly seasonal character of the recession from the October peak, suggest that this may be the case. Even in the worst breakdown of trade relations ever known, ways are being found to supply the minimum needs of food, clothing and shelter, and in the most difficult situation ever faced there are still companies which have been able to put their affairs in shape to do business at a continuing profit. This is a hopeful augury against further decline, and undoubtedly a continuation of the present period of stability in trade even upon the low level would extend to prices, generate confidence and promote investment and business enterprise.

Trade and Industrial Conditions

The chief interest during the past month has been as usual in the holiday retail trade, which has suffered from the reduction in purchasing power and the increased strain upon their resources felt by all classes of people. Dollar sales of the New York department stores are estimated at about 25 per cent less than last year, and as their prices are about 15 per cent lower this figure represents a smaller volume of merchandise sold. Reports from other cities make a similar showing.

December is not as a rule expected to furnish any very stimulating news from the industries, and the seasonal decline has been evident for the most part except in the automobile industry, which has been busy turning out new models to stock dealers for the coming season; evidently its production has nearly doubled the November output of 61,000. The automotive takings of steel, however, have not prevented a decline in steel mill operations from an average of 18 per cent of capacity in November to 13 per cent in the latest week reported, according to Iron Age.

Activity has been better sustained in the textile mills than elsewhere, and of all the industries only in textiles and shoes were factory operations toward the close of the year greater than one year ago. The shoe industry has been a leader in making a product to sell at a price fitting the reduced incomes of its customers, and in October produced 32,973,753 pairs compared with 25,380,808 in the same month of 1931 and 27,731,000 in October, 1930. The employment index for the industry in November was 72 per cent of the 1926 average, compared with 68 in November last year; thus the policy of fitting the shoe to the market is giving employment and keeping up the purchasing power of a substantial group of industrial workers.

The most unsatisfactory development in the situation has been the renewed decline of commodity prices, the weekly price index number of the Bureau of Labor having made a new bottom at 62.5 on December 24, against the previous low of 63.7 on June 18. Livestock and the grains, silver and copper have led the movement. There are special explanations in the case of livestock, where cheap corn has promoted feeding and increased shipments competed with the holiday poultry supply, and in copper, where the effort to arrive at an accord upon production for 1933 broke down upon the insistence of the low-cost African mines, which claim they had no part in building up the present surplus, on larger quotas. Otherwise the price weakness has been a reflection of the disorder in trade relations and in currencies. It is an international problem, and its cause will be removed only when the cause of the trade disorder is removed.

Unbalanced Relationships

In considering what conditions are likely to prevail a year hence the chief anxiety is the extent to which the governments and people will accept and act in accord with the economic principles which are the basis of a highly organized society. The fallacious arguments employed in former depressions are being put forward as reasons for seeking some other way out of this one than the way of trade and price adjustment, but no ground exists for believing that there is any other way. It is stated that the price level will not recover, or that the world is all developed and there is less work to be done, or that the machine has put men permanently out of work; and these are given as reasons for tinkering with the money standard, or for employing the other panaceas proposed. None of these arguments is new to economic history. They regularly recur in every depression, and are as regularly refuted by the outcome. The responsibility for present conditions does not belong to the gold standard or the monetary system, or to any other of the facilities which civilization has evolved to raise its living standards, but to the disruption of ordinary trade and price relationships, and the remedy is not through altering the facilities but by removing the causes of the disorder.

Organized society is essentially a cooperative system of subsisting upon an exchange of goods and services between its individual members. It is a voluntary system based upon individual freedom, and when the accustomed basis of exchange is destroyed and the flow of trade is disrupted the exchanges must be restored by the cooperation of the mem-

bers of the society, both as individuals or, where joint action is necessary, through governments. Continuing adjustments to that end are plainly necessary, and through both channels. The Federal budget needs to be balanced if confidence in the bond market is to be restored and the flow of capital through that market to the industries resumed. Economies in all government expenditures are imperative, for the diversion of an enlarged portion of a reduced national income to the government requires the curtailment of expenditures for other purposes and adds to the trade disorder, while the burdens upon the wealth-producers become unbearable.

Evidence of the disordered relationship existing between the two most important groups of the population is given in the Department of Agriculture's calculation of the ratio of prices of farm products to prices of what the farmer buys, which in November was 51 per cent of the pre-war average, compared with 59 per cent one year ago. The decline in this ratio was checked last June, at the low point of 48, and there was a recovery to 55 in September, but since then the trend has been downward again. This is the chief of those inequalities in the price structure which are reducing buying power, and it reflects the lack of balance between wages in the industries, transportation costs, the cost of government and other items affecting the prices of goods offered, on the one hand, and the returns to the farmer and to farm labor, on the other. The situation is illustrated in the article entitled "A Lesson from the Milk Industry," appearing elsewhere in this issue.

The most frequent approach to the problems presented by this price disparity is through proposals to raise the price of what the farmer sells, but the soundness and efficacy of these proposals is extremely doubtful, and in any event the gap must be narrowed from the other side. The items in industrial costs that do not give way as readily as the farm markets do should be the point of attack, since the inflexibility of these costs is prolonging the disruption of trade from which all are suffering. The inability of the farmer to buy is keeping factory workers out of employment, and the unemployment goes around the circle.

The Railway Wage Agreement

The railway situation is a factor in the lack of balance between the industries and the farms, as well as a very important factor in the economic situation generally in view of the widespread investment of the nation's savings in the securities of the railways. Railway rates are higher than before the war by about 45 per cent, according to the latest statistics of the Interstate Commerce Commission, whereas the prices of nearly all farm products are substantially lower than at that time. This disparity is an influence contributing to the loss of trade and the loss of traffic to the roads, as a result of which 40 per cent of the normally employed railway workers are now out of employment.

The principal factor in the rise of railroad rates over 1914 has been the rise of wages. Between 1914 and 1932 the average wage of railway employes increased 157 per cent, from which level a temporary reduction of 10 per cent was agreed upon last February. This arrangement now approaching expiration, the wage scale has been the subject of negotiation and a new agreement during the past month. It was a condition of the 1931 agreement that the higher rates should be restored automatically in one year, and the employes claimed that it would be a breach of faith for the railway executives, while working under the arrangement, to start action for a reduction under the railway wage act. They sought to impose a condition prohibiting such action as the price of a new agreement continuing the 10 per cent cut. However, the plan finally accepted extends the cut nine months, while either side will have liberty after June 15 to apply for a change in rates under the act.

This is a beginning toward a real settlement. With wages in all industries declining and the railway situation continuing critical, the brotherhood leaders doubtless are reconciled to the probability of a decision against them if the case goes to arbitration and may consider it better tactics not to push the issue to that extreme. It is in the interest of the railway employes as of everyone else that railway costs shall be reduced sufficiently to enable railway rates to be reduced. Not only does the public need transportation charges more in harmony with the price level, but the railways need them in order to compete against other forms of transportation, and the employes need them if they are to have work.

The American Federation of Labor takes the position that the solution of the unemployment problem is through the six-hour work-day and five-day week, but the Interstate Commerce Commission, after making an investigation pursuant to a resolution by Congress, has reported figures with respect to the cost of this proposal if adopted by the railroads which should dispose of it for all the industries. The initial effect, the Commission states, would be to increase operating expenses by $630,000,000 a year, based on 1930 traffic. This proposal is advocated on the ground that it would increase the purchasing power of the railway employes, but manifestly if rates were increased to cover any such cost there would be further disruption of trade, and further loss of traffic. It may be asked how much employment the rail-

ways could continue to give under these conditions? Also, where would the $630,000,000 come from?

Wage rates are a factor in purchasing power, but unless employment can be given they are only a nominal factor; and it is more important to realize that they are also a factor in prices and that unless price relations are kept in adjustment there is no way to prevent a decline in trade and hence in employment.

There have been other developments in the wage situation, including a reduction of 10 to 30 per cent by the Interborough Rapid Transit Co., now in receivership. The assent of the union was given to this reduction, affording an illustration of understanding and cooperation which promotes adjustment to new conditions and saves the waste of industrial conflict. There is no solution to the problem of restoring economic relationships except by the cooperation of individuals, and the more evidence there is of such cooperation the more a hopeful view for the coming year will be justified.

The International Situation

The foreign debts to the United States Government have been the leading subject of interest in the last month, and the developments regarding them have been of a disquieting character. On all accounts it is deplorable that so grave a state of misunderstanding should arise between the peoples of important nations as that which exists between the people of the United States and the peoples of these debtor nations. For the differences are not merely between governments, but the uppermost subject of discussion in all the countries concerned, and there can be no question that on both sides the policies of the governments have been supported, even demanded, by public opinion. There is good reason to believe that the governments would adjust the differences by mutual concessions but for the pressure of public opinion against concessions. This is a state of affairs that in other times might have led to war, but fortunately nobody wants to resort to arms over this situation. However, in modern life there are many ways outside of formal war in which animosity may be manifested, and injuries inflicted. It is deplorable that animosity should exist and be cultivated between these peoples. This is especially true now when there are so many ways in which cooperation is needed to promote the interests they have in common.

In the first place, it is clearly quite impossible for the body of the people on either side of the debt controversy to put itself mentally in the place of the body on the other side and see the situation from that viewpoint. M. Herriot, the late French Premier, is eminently a fair-minded man and a sincere friend to the United States. He made a courageous struggle to accomplish the French payment, but Americans who have read his gallant speech to the Chamber of Deputies have been impressed that even he has failed of understanding the views of the mass of the American public upon the war and the debts and (as seems to Americans) the consistent policy of the United States Government on the subject from the beginning. The speech upheld the French claim for a reconsideration of the debt settlement, but urged that the pending payment be made and the desired relief be sought thereafter through friendly representations. He failed to persuade the Chamber but was satisfied to retire from office on that issue. He wanted a settlement by mutual understanding, and this is what every right-minded person on either side of the controversy must desire, for contrary to the off-hand opinions of many people, the problem involved is an extremely complicated and difficult one.

It is unfair to assume that the debtor governments are indifferent to their obligations and have no motive but that of avoiding a burdensome payment. They urge that in the present state of the world economy these payments tend to disturb all trade and financial relations and thus delay the restoration of normal production and employment, which is a matter of far more importance to every country concerned in these debts than are the debts themselves. We should be sure that we give proper weight to these representations, for they are backed by the opinions of able and impartial economists in all countries.

The Problem of International Payments

Without doubt there is general failure to understand the peculiar difficulties which attend at this time upon payments which must be made from one country to another, and from one currency to another, in contrast with purely domestic transactions. It is frequently said that it would be unfair to domestic debtors for the United States Government to take any action for the relief of the debtor governments without doing something of equal value for the relief of domestic debtors, and that action in behalf of the former would increase the difficulties of the latter. It is important to understand the difference between the two situations.

A debtor anywhere must first gather together the funds required for the payment in prospect, and it may be assumed that this procedure is about the same in all countries. In the case of a domestic transaction this is practically the end of the task, for the bank credit or currency in the debtor's possession is turned over to the creditor. The foreign governments

indebted to the Government of the United States receive their revenues in their own currencies and pay their domestic obligations in those currencies, but obviously the debts to the United States Government cannot be paid with those currencies. They must be paid in United States currency, and to this end credits —bank balances—must be acquired in the United States. There are only three ways in which this can be done: (1) by shipping gold, which is acceptable because gold is the basis of our monetary system; (2) by acquiring bills of exchange drawn against importations of commodities or securities into the United States; (3) by borrowing the required sum in this country. Since the third method is impracticable at the present time, it may be eliminated, leaving only the two other methods. For the moment we will pass the gold method to be considered later, for it is practicable to only a limited extent. The great bulk of international payments are made by means of bills of exchange, as the great bulk of domestic payments are made by means of bank checks. In either case the instruments are drawn against existing bank balances or values moving in the course of business. In order to discharge their obligations the debtor governments through their bankers must proceed to acquire bills of exchange, which, as we have seen, represent claims on banks or business houses in the United States.

Thus we have the basis for the proposition laid down by economists and all persons who are familiar with exchange transactions, that large international payments can only be made by means of goods and services.

At this point account should be taken also of one of the difficulties which the debtors meet in seeking to make these payments, to-wit, that it is the policy of the United States to restrict importations of commodities rather closely to goods that are not competitive with the products of this country. In a general way the industries of the debtor countries are quite similar to our own, and their products are largely competitive, which obviously handicaps them in their efforts to accumulate credits in this country. They must to a great extent resort to what are called triangular transactions, i.e., they must acquire exchange on the United States from countries which have surplus balances in trade with this country. Of course this process is made more difficult by the heavy decline in the volume of world trade due to the business depression.

That these difficulties incidental to the acquisition of exchange on the United States are not generally appreciated is evident from comment frequently heard. We have mentioned in the past the rather crude witticism that the German people could make the reparation payments if disposed to do so by each drinking one glass of beer less per day, and have called attention to the fact that if the German people abstained from beer completely it would make no difference in their ability to pay reparations unless the creditor countries would receive imports of beer and permit the application of the proceeds of the same upon that account, or admit other commodities which abstention from beer had enabled the German people to produce or purchase.

A similar reply may be made to the common observation that the debtor nations could make their payments to this country by reducing their expenditures upon armaments. If they ceased all expenditures upon armaments their ability to make the debt payments would not be increased unless the labor that had been employed upon armaments could be employed in the production of goods which would be admitted into the United States, or which might be exchanged for goods which would be admitted into the United States. The essential point is that payments of such magnitude can be accomplished only by transfer directly or indirectly of movable property of some kind to the creditor country.

Great Britain's Gold Payment

Great Britain, having decided to make the payment of $95,550,000 due on December 15 last, elected to make it in gold, and her reason for so doing, instead of making payment in exchange, illustrates the entire problem. In normal times payments across international boundaries have been made by bills of exchange, except that from time to time exceptional one-way movements of commodities or securities have occasioned moderate shipments of gold for the settlement of balances. In the entire history of this country prior to the war there were only two years in which our net importations of gold exceeded $100,000,000. The gold shipments served to maintain a common international basis for all currencies, thus affording a firm basis for prices and trade. Movements aggregating as much as $100,000,000 were unusual because ordinarily international transactions practically cancel and settle themselves in the clearings, as in the case of domestic payments. Indeed it has been demonstrated that stable relations between the world currencies are impossible unless such is the case. Exceptionally heavy drafts upon the gold reserves of any country will require drastic contraction of credit in that country, which inevitably precipitates a crisis.

Unfortunately, in recent years, by reason of numerous derangements in trade and extraordinary payments of various kinds, (reparations and debts accounting for some of them), the balances calling for gold have been so heavy that 45 nations have found themselves

obliged to suspend gold payments. In the absence of this stabilizing tie the currencies all began to fluctuate in relation to each other, exchange rates varying with day-to-day demands, and the effects upon international trade have been so disastrous that a general call for an international conference upon the subject has arisen.

At first it was proposed to hold such a conference immediately following the British Imperial Conference at Ottawa, but by that time the approach of the December 15 debt payments to the United States moved the debtor nations to desire that the conference be postponed until after that date. Since then no steps have been taken, for obvious reasons.

Position of Great Britain

Great Britain suspended gold payments on September 21, 1931, and her currency has been fluctuating in relation to gold ever since. Reckoned in dollars, the value of the pound sterling at the old par was \$4.8665, but by December, 1931, it had declined to \$3.25, from which it reached a high in 1932 of \$3.83, then declined to about \$3.47 in early October.

In the latter part of October the movements of British exchange apparently began to feel the influence of apprehensions regarding the payment due to the United States on December 15. The acquisition of exchange on New York would mean that pounds must be offered for dollars, which would tend to depress the former and raise the latter. The market rate of the pound in dollars declined gradually and with fluctuations, from \$3.47 to about \$3.30 early in November, and then, as concern became more acute, to \$3.20, and finally a low of \$3.14½ on November 27. At the former fixed par between the two currencies the equivalent of the above sum of dollars was £19,630,000, but acquisition of the required amount of exchange at the low point would have required £30,381,000 of depreciated currency or a premium, of 55 per cent. This premium of course would not have gone to the United States government, but to the sellers of dollar exchange in the markets. Presumably on account of the prospective cost to the Treasury, and the possible effect of such purchases upon exchange rates, the British Government decided not to acquire exchange, but to make the payment in gold obtained from the Bank of England's reserves. Upon this announcement the market value of pounds in relation to dollars recovered rapidly and is now above \$3.30. No doubt the choice was best for immediate results, but it involved the position of the currency for the future. The payment reduced the gold reserve of the Bank of England to 23.6 per cent of its demand liabilities. The last statement of the Federal Reserve system shows a reserve of 62.7 per cent.

Effects of Exchange Fluctuations Upon the United States

Perhaps by this time the reader is mentally commenting that while these fluctuations of the British currency are doubtless regrettable, he does not see that they constitute a problem that is up to the United States, which has problems enough of its own. This, however, is to ignore our relations to world trade, and the fact already set forth that debt-payments are dependent upon world trade. The fluctuations of the pound sterling are important everywhere because they both influence and illustrate the confusion in all of the exchanges. The pound sterling has been for a long time the most important monetary unit in the world's exchanges. More bills of exchange have been drawn in pounds sterling than in any other money; more transfers take place between other currencies and the British currency than between all other currencies and any other one currency. London has been the clearing house of the world. Therefore, instability in the pound sterling exchanges have far-reaching effects.

Let it be supposed that instead of making the December 15 payment in gold the British Government had chosen to acquire bills of exchange on New York, and to make the example concrete, let it be supposed that it acquired a round sum of such bills from Brazilian coffee dealers who by shipments of that commodity had created credits in New York. These credits originally afforded means of making purchases in the United States, but when exchanged for credits in London they would become available for purchases in Great Britain. In this case we would obtain the debt payment but lose the trade.

More serious than this, however, would be the combined effects of all the bids for exchange on the United States in depreciating the exchange value of other currencies in their relations to the currency of the United States. In prosperous times, when the total volume of the exchanges is large and rising, the demand for the debt payments might be absorbed without serious disturbance, but recent fluctuations of the pound sterling are obvious demonstrations of this influence under present conditions. The effects of rising rates for dollar exchange are seen in all branches of our foreign trade. They explain why, in competition with wheat quotations in Canadian, Australian or Argentine currencies, our total exports of wheat and the equivalent of wheat in flour from July 1 to December 10 this season totaled only 23,888,000 bushels, compared with 75,766,000 in the previous season, whereas Canada's exports (four markets) increased from 117,533,000 to 175,156,000 bushels. Describing the ship charter market, the London Times of December 10, made the following statement:

Shipments of Australian Grain

The week in the freight markets has been distinguished by activity in the export grain trade from Australia, and many vessels have been chartered for voyages to both Europe and the Far East. The large buying of Australian grain has been encouraged by the exchange situation and by the consideration that at this period of the year the competition of other varieties of wheat is not so keen. The St. Lawrence season is now closing—the last grain-laden vessel has sailed from Montreal this week. The export of grain from the United States continues to be restricted by the adverse rates of exchange, and recently the United States has, from a cargo ship-owners' point of view, receded into the background of the freight markets. The drop in the export of American commodities in bulk seems to have been accompanied by a decline in the shipment of general merchandise to this country, which has been indicated in a falling off in a demand for vessels on time charter and in a preference for smaller ships, whereas in the past larger vessels have been wanted by the chartering firms. Business men are not at all surprised by the decline in American exports in view of the increased cost of United States merchandise owing to the unfavorable exchange.

In the past both the United States and Canada have had considerable sales of wheat and flour in Asia, but an effect of the confusion in exchange rates is seen in the fact that this year both countries have been eliminated from that field by Australia, whose currency rates are lower than those of either of the other two countries.

The discount on the Canadian dollar, and the new tariff rates, are together having a very depressing influence upon our trade with Canada, and one curious effect reported is an increase of American ocean travel by Canadian steamship lines, due to the fact that Canadian currency can be used to accomplish a reduction of fares.

Furthermore, the effects of depreciated foreign currencies are seen not only in our loss of exports, but in the aid thus given foreign competitors to place their goods in our market. The Tariff Commission is busy with appeals for help from the domestic industries against this intrusion, and President Hoover recently has approved recommendations by the Commission for higher duties in a number of cases. Reports are current of American manufacturers who are considering the possibility of producing abroad to supply their regular trade in this country.

The effects of depreciation in the principal exchanges were not important prior to about the middle of 1931, and since then these effects have been minimized by the moratoria that have been in force. They are a new and additional element in the exchanges, but already their influence is distinctly observed. The instability of the British currency has been a marked feature of recent months, and has been directly related to the December 15 payment. It is to be considered that the aggregate reduction in the volume of this country's foreign trade since 1929 (approximately 70 per cent) is so great that obviously the influence of equal purchases of dollar exchange now would be very much greater than in former years.

Competitive Currency Depreciation

There can be no question that depreciation of currencies has brought into trade a new and demoralizing competition. It is sometimes suggested that the United States should join in this competition to protect itself from the consequences to its trade, and should therefore cut loose from the gold standard and depreciate the dollar, but this only illustrates the infectious character of dangerous ideas. In Great Britain, as is well known, there are many advocates of a cheaper pound, and in Canada of a dollar cheapened in relation to the pound.

The theory that a country strengthens its competitive position by depreciating its money is deceptive and utterly unsound. One country adopting this course may gain a temporary advantage in export trade by offering goods at the same nominal price in cheaper money, but once the competition is entered upon there is no stopping place short of the zero point for all. It is the most uncontrollable, demoralizing and fruitless competition that can be imagined.

There can be no gain in the competitive capacity of a country by cheapening its money, except as some factor in production may have its real compensation reduced in the shuffle. If labor is willing to receive the same pay in a money of lower purchasing power, costs and prices can be reduced to this extent.

The Union of South Africa, which is the chief gold-producing country of the world, is reported to have abandoned gold payments within the last week. The Mine Operators' Association has been urging this course ever since Britain left the gold basis, for the scarcely concealed purpose of effecting a reduction of wages. If the gold output sells at the present premium of gold over the sterling currency, (about 33 per cent) and mining wages can be paid in the depreciated currency at the same rates as heretofore, the gain to the mining companies will be important. It is urged that the life of many of the old mines can be substantially prolonged by the change.

The price changes resulting from a depreciated currency may come so gradually, especially in a time of depression, as not to be noticed for some time, but this is pure deception. In the long run all relations tend to make corresponding readjustments, although there never can be complete compensation for the injustices that result.

All Countries Wanting Stabilization

All of the countries whose currencies are depreciated and fluctuating under varied influences, including the manipulation of speculators, are anxious for some constructive action to stabilize the exchanges, but there is no denying the fact that the war debt payments are everywhere regarded as a menace to all efforts

of this kind. At this time men of understanding everywhere are asking each other whether, if the attitude of the United States is unalterable, an international conference is worth while. Have we made such a thorough study of this subject as warrants our saying that there is no ground for such fears?

If Great Britain had chosen to make the last payment by gathering up exchange on New York over the world it is probable that sterling rates would have gone still lower, which means that dollar rates would have been forced still higher, increasing the handicap under which our products already labor in foreign markets.

The policy of Britain in making payment in gold was dictated by unwillingness to thus depreciate her currency further, while paying an enormous premium for the exchange. Her intimation that she cannot continue in the future to pay in gold cannot be intelligently discounted, for in the present state of industry and trade she has not the means of acquiring such amounts of gold.

The Actual Difficulties

We have endeavored to set forth, not a discussion of all the rights involved in the debts controversy, but some of the practical difficulties which involve attempts to pay great sums across international boundaries in the present disorganized state of world trade and world monetary systems.

We are obliged to recognize that these debts were not created by shipments of gold to Europe, but by sale of our products at war prices; also that as a people we are opposed to accepting payment in products which would displace the products of our own industries; also the increased difficulty of obtaining dollar exchange for these payments, as a result of the heavy decline in the volume of our foreign trade; and finally that if the debt payments have the effect of creating greater confusion in the exchanges and lower prices for our farm products their effects upon American debtors would not be helpful, but injurious.

Evidently this country is an important factor in the present world situation. We are insisting upon the performance of agreements which, whatever the original equities may have been, are said to be now a bar to cooperative efforts for the reestablishment of order. Are we able to deny the truth of these representations?

Finally, what policies are open to this country and what results may be expected to follow upon them respectively?

If there is no stabilization of the currencies the efforts of the debtor countries to make payments in exchange may be expected to increase the disorder in the exchanges and the depreciation of the currencies, the effect of which must be to practically compel our abandonment of foreign trade. We would have to resort to a veritable tariff wall of exclusion to protect the home market from a kind of competition that while it lasted would be utterly unfair and destructive. In other words, we would have to take a distinctively defensive position, and endeavor to reform our economy with a view to living within ourselves in the future. We are aware that not a few people consider this to be a practicable policy, but we cannot think they have any adequate idea of the extent of the readjustments that would be required, the length of time they would require or what the cost would be. Moreover, it is certain that there would be no collections on the debts. In our opinion the proposal is impracticable and futile, and would deny the natural ambitions of an enlightened and progressive people.

Another course would be to adopt monetary depreciation ourselves and endeavor to keep up with, or a little ahead of, all competing depreciations while the game lasted, until all the world arrived at the plight which Germany reached in 1923, without stopping to think who would perform the rescue act which the Dawes Commission and Germany's creditors performed in 1924 by the reestablishment of a sound monetary system in order that Germany might pay reparations. We look upon this proposal as we would upon one to have a boat race over the Niagara cataract.

There remains the opportunity to gain a stabilization in the price structure of goods moving in international trade through those efforts that would result in the reestablishment of the monetary systems of the world, and especially of those countries with which debt adjustments may be made, to the end that such currencies may attain a gold basis and have a direct and continuing relationship to the dollar. We offer no plan for settlement of the debts, but any adjustments that are made should be such as to give full promise of the accomplishment of this purpose, as we believe it to be a fundamental factor in our own recovery.

Money and Banking

A further increase of $167,000,000 in the monetary gold stocks of the United States was the most important banking development during December. This more than offsets the losses of the Spring and establishes gold holdings at a new high point for the year. The principal factor in the increase was the payment on December 15 of $95,550,000 in gold by the British Government on account of war debts. The balance of gold gain included shipments of $31,420,000 from Great Britain apart from payments on the war debt. Towards the close of the month, the weakness of French exchange re-

sulted in imports of $9,000,000 from Paris, the first actual movement of gold from that center to New York since April, 1931. In addition, it is reported that $9,000,000 is en route from France.

Reflection of the payment by the British Government to this country appeared in the Federal Reserve statement of December 21. Upon request of the Bank of England, the Federal Reserve Bank of New York arranged to place at the disposal of the Bank of England on December 15 gold to the value of $95,550,000 against an equivalent amount of gold to be earmarked for the account of the Federal Reserve Bank of New York in London pending shipment to New York. On December 15 the Bank of England instructed the Federal Reserve Bank to pay the gold to the United States Treasury, which in turn redeposited the gold in the Reserve Bank, receiving in return a book credit against which it drew in connection with its own public debt payments on the 15th. Meantime, the gold itself is being carried on the books of the Reserve Banks as "gold held abroad" and is included in the monetary stocks of the United States, though not in the reserves of the Reserve Banks, which, according to law, must be held in this country. Gradually, as shipping space becomes available, the gold will be transported.

Abnormal Accumulations of Funds

The effect of these payments and of gold imports to the United States was to add further to the already redundant bank reserves of this country. Ordinarily, in the month of December, there is a large expansion of currency in use by the holiday trade, which, in other years, would have offset a considerable gold inflow at this season. But this year the demand from this source has been considerably smaller than usual, with the result that the cash balances of the member banks at the Reserve Banks have gone up to the highest levels since June a year ago. Inasmuch as the deposit liabilities of these banks have greatly shrunk over the past year, it is apparent that the banks are the possessors of far larger reserves than they can find safe and profitable use for under present conditions. For the member banks alone the total of this "excess" alone is estimated at substantially above $500,000,000, or enough to support a volume of bank credit approximately $5,000,000,000 larger than at present, and with the figures of the non-member banks included the total would be much larger.

The existence of this huge store of idle funds is the dominating feature of the money markets. It explains the unprecedentedly low rates for prime short-term investments, but beyond that it demonstrates completely the futility of the claim occasionally heard to the effect that the country is suffering from a money shortage. Clearly the volume of funds awaiting the beck and call of business is enormous. In view of the magnitude of the excess funds already built up, the question is worth considering whether the interests of the country are best served by adding further to these sterile gold stocks or by cooperating in every way possible with measures designed to improve world trade and put these idle stocks to work.

Bond Market Improvement

The action of the bond market has been more encouraging during the past month in that the declining tendency of previous months was less in evidence and prices in a number of departments displayed notable strength. High grade issues were particularly favored, due apparently to absence of any year-end monetary strain and to other indications of continued plethora of funds. United States Government issues were leaders of this group, a number of the larger issues showing advances ranging 1 to 2 full points to new high levels, while Treasury one-year certificates reached price levels reducing the yield to less than ¼ of 1 per cent.

New York City bonds responded to the measures taken to protect the City's credit (discussed elsewhere in this Letter) by rising to new high points for the year, and other high grade municipals were in demand. In the foreign list, German Government obligations were especially strong, reflecting increasing confidence in the economic progress of Germany. Second grade domestic rails, on the other hand, were generally soft under the influence of fears of impending reorganizations or receiverships.

Of significance are the figures in the following table showing the drastic shrinkage that has taken place in the volume of corporate financing during the past two years. The figures are of interest, not only for their bearing on the demand-supply situation in the investment markets, but likewise for what they show as to the rate of capital investment in industry. In this decrease lies both an explanation of the depression of the present and the basis for the recovery of the future.

Corporate New Capital Offerings*
(In Million Dollars)

Calendar Year	Railroad & Public Utility	Industrial & Related	Land & Buildings	Investment Trusts & Misc.	Total Issues
1925	1,861	1,098	716	426	4,101
1926	1,944	1,196	710	507	4,357
1927	2,571	1,281	630	909	5,391
1928	2,176	1,407	716	1,781	6,080
1929	2,479	1,928	520	3,712	8,639
1930	3,162	1,071	245	466	4,944
1931	1,294	273	129	67	1,763
1932**	290	9	8	11	318

*Source—Commercial and Financial Chronicle.
**December figures preliminary.

New York City Finances

Progress towards the solution of the financial difficulties of the City of New York has made rapid headway during the past month. Impelled by the crisis in the City's affairs because of inability to provide ready money for pressing maturities and other obligations, the Board of Estimate and Apportionment of the City passed a resolution on November 30 asking for a special session of the State Legislature to authorize the City to take certain steps to reduce its cost of government. On December 9 the Legislature was convened, and on the morning of the 15th adjourned after having taken action as follows:

(a) A bill had been passed to authorize the City authorities to reopen the budget for 1933 for the purpose of making further reductions therein;

(b) Another bill had been passed to authorize temporary reduction in teachers' salaries;

(c) The third bill had been enacted into law empowering the City generally to reduce the salaries of its employes; and,

(d) A resolution had been adopted setting up a legislative committee to take steps toward revision of the City's charter by the regular session of the legislature in 1933.

The Origin of the Difficulties

By this legislation the way is now cleared for the City to deal effectively with its financial problems. For over a year these problems have been a source of growing concern to bankers and the investment market generally by reason of the tardiness of the City government to recognize the imperative necessity of adapting its financial policies to the exigencies of the time. At bottom the difficulties with which the City has been contending are the same as those facing all governments, and most business concerns and individuals. They are difficulties of adjusting ideas, habits and general scale of living to reduced incomes. Such adjustments, difficult enough for business concerns and for the individual, are doubly difficult for governments because of the enormous weight of the political influences involved.

During the period of rising business activity and prices, the expenditures of New York City, in company with those of the American people generally, underwent a large increase. With prosperity and abundant revenues came a natural demand for extensive public improvements voted by a rich and growing community. The number of office holders increased and wages and salaries of public employes rose in conjunction with the general rise of the cost of living. Things were done on a broad scale, and the cost of government steadily increased, as shown by a rise in the budget from $351,000,000, exclusive of capital outlays, in 1922 to $631,000,000 in 1932, and in the net funded debt from $1,067,000,000 to $1,737,000,000 during the same period.

Mounting taxes, paid with relatively little protest while income from property held up, have become a serious burden as vacancies in business and residential properties have increased. Real estate values have fallen, forecasting a further decline in assessed valuations and in the general property tax which constitutes the principal source of City revenue. The collection of taxes has lagged. In the face of general deflation in other fields of business, New York City expenditures continued to increase throughout the first two years of the depression, with the result that the 1932 budget was the largest on record and the City at the beginning of the year was still contemplating a building program that would cost in excess of $1,500,000,000 over the next decade. The same disregard of basic economic conditions was characteristic of municipal finance generally throughout the country.

The Crisis of Last January

With large maturities falling due in January a year ago, in addition to the usual running expenses, the City at that time found the investment markets in so unsatisfactory a state as to practically preclude the possibility of a refunding operation. In this emergency the City called in representatives of New York banks to cooperate in formulating a program for raising the necessary funds. The bankers made a careful study of the situation and agreed to furnish the required monies providing the City would definitely engage itself to a policy of economy and retrenchment needed to reestablish its credit on an assured basis. This the City promised to do, making public declaration of its intention in a resolution passed by the Board of Estimate on January 20 which read in part:

The City Administration shall forthwith undertake measures to curtail and postpone its plans and undertakings; shall seek in every way to reduce the cost of its present activities, and shall endeavor to limit new projects to those which are self-sustaining in order that the City may more effectively employ its resources in serving the vital needs of the people; and

That studies will be promptly undertaken with the purpose of developing new sources of revenue and of determining what present activities of the City may be put on a totally or partially self-supporting basis; further that each department head is hearby directed to submit his plan in accordance with the terms of this resolution and as promptly as possible to make a report to the Mayor on such suggestions or plans.

Economy Promises Ignored

Thus, the situation was temporarily eased and there was a substantial recovery in the prices of City securities. Aside, however, from the postponement of approximately $215,000,000 of public works, very little was done by the City to carry out the promise of economy. At the same time, the revelations of the Seabury investigation during the Summer, together with the action of the Board of Estimate in checkmating the economy efforts of

Acting Mayor McKee, were decidedly damaging to the City's credit, and raised a question in the minds of investors as to the seriousness of the City's intentions to put its finances on a sound basis. And these doubts were further increased by the action of the Director of the Budget on October 5 in bringing in a budget for 1933 calling for a reduction of only $16,717,385 from the record figure of 1932.

It was at this point that the City was obliged to call upon the bankers for the second time during the year. On October 13 Comptroller Berry asked the City's principal bankers, the Chase National Bank and The National City Bank, for a loan of $35,000,000 for the purpose of meeting pressing requirements, including payrolls and unemployment relief. This request was refused by the bankers, pending further reductions in the budget, and in consequence of this refusal the Board of Estimate adopted a revised plan of subway financing, extending $104,000,000 of four-year subway bonds held in the City's sinking fund to fifty-year maturities, thus reducing the current charges on the budget by approximately $50,000,000. This, together with other accounting changes and minor cuts in expenditures, effected a net reduction of $56,000,000 from the budget as first proposed to $558,407,000.

While these reductions were not regarded as satisfactory by the investors or civic organizations generally, the bankers agreed to finance the City's requirements for November estimated at approximately $21,000,000, including unemployment relief. At the same time they called attention to the failure of the City to keep its promises with respect to economy, and declined to make any commitments beyond November.

Thus the situation remained at stalemate until the close of the month when the prospect of approximately $151,000,000 of revenue bills maturing, together with other current obligations, impelled the Board of Estimate on the 30th to ask for a special session of the Legislature, at which the economy bills were speedily enacted into law as outlined in an earlier paragraph. The way was thereby paved for budget reductions and the bankers are financing the City temporarily, pending the promised reductions in the 1933 budget, which should reassure and satisfy the investing public to a point where securities of the City can again find a market on a creditable base.

Attitude of the Banks

Because of constant misrepresentation on the subject, it is in order to make clear the attitude of the bankers in negotiations that have taken place.

The bankers do not attempt to concern themselves with the administration of the City affairs nor to say where money shall be spent or shall not be spent. It would be an impropriety for the bankers to dictate just where savings in the budget should be made. They have not done so and they have no intention of doing so. Their concern is purely the credit standing of the City, where their responsibility is two-fold; first, to those investors who through the bankers have purchased hundreds of millions of the City's obligations; and, second, to the City, to which they attempt to reflect the attitude of the investing public whose confidence in the City is essential in its necessitous future borrowings.

The first and foremost requirement for the maintenance of credit is a balanced budget; that is, an equalizing of expenditures with the reasonably to be expected income from tax levies. Under existing circumstances tax levy expectations are lower and therefore expenses must be lower. Because the City authorities have failed to attack this problem with sincerity, the result has been that the City's credit has substantially ebbed.

The closing of the 1933 budget without impressive economies brought the City face to face with the fact that potential buyers of the City's securities, by which is meant insurance companies, savings banks, trustees of estates and individual capitalists, lost confidence to a point where they refused to purchase additional securities and threatened to throw into the market City securities which they already held. As a result bankers were obliged to say to the City authorities that there must be further reductions in their expenditures.

About sixty per cent of the expenses of the City are for personal services and unless that item could be reduced any substantial reduction in expenses was impossible. The City authorities showed that over two-thirds of the cost of personal services was controlled by mandatory State legislation and contended that that item could not be touched since any reduction of salaries and wages not controlled by mandatory legislation—this being the smaller part—would be looked upon as grossly unfair unless the larger body was similarly affected. The obvious answer of the bankers then was that there seemed no alternative but to ask relief from the State Legislature from the mandatory legislation, to the end that there could be some reasonable economy obtained in personal services, and further to ask for a reopening of the budget to the end that there might be other savings established, it being clear that it would be necessary to take at least a $40,000,000 cut in the budget to assure that balancing process which alone could satisfy the skeptical investor.

The Basis of New York City's Credit

Backed by the wealth and resources of the greatest city of the United States, there is no question as to the intrinsic soundness of New

York City issues. Even with the slowing up of tax collections, the total taxes received by the City for the year up to and including November 30 were only about 7½ per cent less than those collected for the corresponding period of last year. Though it be admitted that these levies represent an undue burden upon the taxpayer under present conditions and must be reduced, nevertheless the relative stability of New York City's sources of revenue, compared with the fluctuations in income of corporations and individuals generally, makes a remarkably fine showing. It is significant also that New York City taxpayers contribute 75 per cent of the revenues received by New York State, yet the latter recently sold an issue of $30,400,000 one to fifty year serial 3 and 3¼ per cent bonds. The long maturities were offered to the public at prices yielding 3.15 per cent. This compares with a yield of 4.75 per cent on outstanding comparable New York City issues. The problem, in other words, is not primarily one of income. It is a question of good management and of firm intention on the part of public servants to cut financial garments to suit the cloth,—a policy which alone assures solvency, whether the subject be a government, a corporation or an individual.

Already the City's budget for 1933 has been reduced $74,000,000 from the 1932 total of $631,000,000, and the additional economies of $40,000,000 to which the City is definitely committed will bring the total reductions to $114,000,000. By just so much as the City carries out its promises and evinces a real determination to institute the economies that the times demand, to that extent will its credit be restored to the high place to which it is properly entitled.

North Dakota Votes Down A Moratorium

One of the events of the last election which has not had the publicity which its importance deserves was the action of the voters of North Dakota in defeating by 38,000 majority a referendum proposal to establish a partial moratorium upon indebtedness in that State for the period of three years. In view of the critical state of agriculture and the representations that have been current in Washington about the attitude of the farmers, this vote is sensational as a revelation of the background of conservatism actually existing in the agricultural country.

North Dakota has had several spasms of "progressive" politics in years gone by, and has a variety of unique acquisitions from them of which one is the system of direct legislation known as the initiative and referendum, at one time hailed as the solution of social problems. This movement for a moratorium was "initiated" in the primary campaign last June. It was fathered by the Farmers Union of North Dakota, which secured sufficient signatures to entitle it to a place on the primary ballot. As then proposed it provided for a five-year moratorium on all debts and taxes except conditional or installment sales agreements, and also excepting debtors who could be shown able to pay. The proposal looked formidable, but opposition promptly developed and after a vigorous contest the measure was defeated in the primary by about 18,000 votes.

The Farmers Union then redrafted the measure to eliminate the exemption of conditional or installment sales agreements, and to provide for only a three year "recess" instead of five; cursory mention of need for the "Frazier Bill" (fiat currency) also was eliminated from the later draft. Sufficient signatures were obtained to put this measure on the General Election Ballot November 8th. This time the Farmers Union, at their State convention, in local rallies, through wide circulation of their official organ, the Farmers Union Herald, and by other similar means, conducted an intensive campaign for the measure.

The scope of this measure was as follows:

An act providing a partial moratorium for three years on all existing indebtedness at effective date (December 8), including taxes and debts due by individuals to State, county, and other political subdivisions; except that its benefits shall not extend to corporations, nor to any person who, upon order to show cause before any district court, is found to be able to pay without sacrificing home, lands, or goods and chattels with which he creates wealth for a living or which are necessary to maintain his family.

No official may levy upon, attach, or sell personal property (other than above excepted) under an execution issued upon a judgment or upon any other indebtedness at effective date, for a period of three years, provided only that debtor pays 1% interest annually. Sheriff's deed shall not issue on foreclosure sales for three years, nor may the state foreclose or cancel any land contract provided debtor pays 1% interest and future taxes. Nor may any county issue a deed on any tax certificate now outstanding provided debtor pays 1% annual interest.

Realizing that a large vote would be cast in the presidential election, and appreciating the appeal which the proposal would naturally have under the distressing economic conditions, the opposition rallied for a more determined fight in defense of the good name and credit of the State. The campaign was an intensive one, carried on by posters, pamphlets, newspaper advertisements, speeches and radio. It completely overshadowed the presidential contest, and the result was a more sweeping victory for the forces of conservatism than in the primary election. This is believed to show beyond cavil that regardless of hard times and the specious arguments in favor of lying down on their obligations, the people of North Dakota intend to pay their way through and keep their State's record clear. They know the difficulties, but also know the difficulties of any other course. Their action cannot fail

to exert a wholesome influence throughout the country. These are times that try the mettle of men, and this vote will be a matter of State pride in the years to come.

A Lesson from the Milk Industry

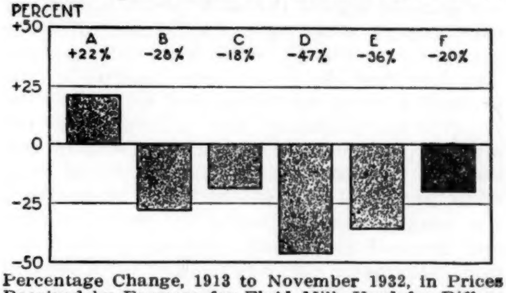
A further reduction in retail milk prices in New York City was announced last month, accompanied by a reduction in the prices paid to producers for raw milk. The production of milk is the most important source of income to New York farmers, and milk and other dairy products are among the most essential food commodities entering into the consumption of the city population. A study of the milk situation in New York therefore is interesting for the bearing the facts have both upon the economic status of an important group of farmers and upon costs of living to the mass of the people in New York City. The study is made more significant by comparing present facts with the corresponding ones existing in 1913, for this illustrates the changes in the relationship between agricultural products and urban products and services generally, and also shows why one of the chief items in the cost of living in the city is approximately 22 per cent higher than in 1913. It illustrates therefore the general maladjustment which is one of the chief factors in this state of depression and unemployment.

Milk Prices

Since 1929 the average price received for all milk by the farmers of New York State has declined from $2.75 per hundred pounds to $1.18 in November, 1932, and is 20 per cent below the average received in 1913, which was $1.47. The retail selling price of standard grade B milk delivered to the family trade in New York City has been reduced from 16 cents per quart in 1929 to 11 cents at present, but as compared with the pre-war price of 9 cents it is still 22 per cent higher.

The comparison usually made is between the selling price for bottled milk and the price received by the farmer for all milk, but such a comparison is misinforming in several respects. Retail sales of fluid milk represent an important but not major portion of the sales of milk for all purposes, at present making up from 25 to 40 per cent of the total. The Dairymen's League Cooperative Association, Inc., whose membership includes a large proportion of the New York State dairy farmers, has had in effect since 1921, by agreement with the milk distributors, a varying scale of prices for raw milk, dependent upon the use to which the milk will ultimately be put. There is a basic or contract price, now $1.52 per hundred pounds (compared with $3.39 in 1929) for the milk sold for retail distribution in bottles, but the surplus of milk over the contract requirements is sold for other purposes at whatever prices it will bring in the competitive markets. In November, for example, the quoted price of the Dairymen's League for milk to be made into cream was $1.06 per cwt. (plus certain allowances for skim milk), for manufacture into condensed and evaporated milk $1.20, for butter $0.78½ and for cheese $0.94½. When the milk for these various purposes had all been disposed of, and the operating expenses and any possible losses of the cooperative association had been deducted, the farmer received a settlement that amounted to $1.18 per cwt. on an average for all milk sold.

The relative change in the November, 1932 prices as compared with 1913, when there was a uniform price, is shown in the chart below:



Percentage Change, 1913 to November 1932, in Prices Received by Farmers for Fluid Milk Used for Different Purposes in the New York Market.

A—For the New York retail trade.
B—For making into cream.
C—For condensing and evaporating.
D—For butter manufacture.
E—For cheese manufacture.
F—Average for all purposes.

It would be unfair to charge against the distributor of fluid milk the difference between this $1.18 and the retail selling price, inasmuch as the distributor paid in November the $1.79 rate for all milk purchased by him for retail sale, which price has since been reduced to $1.52, accompanied by a reduction in the retail price.

Another serious error in the price comparison as usually expressed is the assumption that all of the liquid milk is sold at 11 cents per quart, the prevailing price for the standard grade B milk delivered to family trade. Only a portion of the sales is made in this way, the balance being sold at wholesale in bottles to stores, restaurants, etc., at 8 cents per quart, and in bulk at 32 cents per gallon, and much is sold below these "prevailing" quotations.

The Problem of the Surplus

The figures given above for the varying prices received by farmers for milk, according to the uses to which it is devoted, show that the best price is from the retail distributor, while the manufacturers of condensed milk, cream, butter, cheese, ice cream and other products pay much lower prices for practically the same standard grade of milk. The explana-

tion of this is, first, that the contract supply for the distributing companies must be obtained from a local area, and the price must be high enough to maintain a reliable supply, and second, that the surplus over these contract requirements must be sold on a basis that enables the purchasers to meet the competition of all dairy products coming from other parts of the United States, and at times from foreign countries. The milk companies dealing with the Dairymen's League justify their assent to the policy by their desire to cooperate with the League in efforts to maintain a fair price to the farmers of the New York milk shed and an assured supply of wholesome milk for their trade.

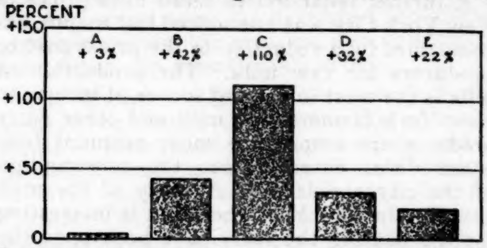
It is evident, however, that the system has not entirely solved the milk problem even for the farmers who have the benefit of close proximity to the big New York city market. The fact that the Dairymen's League is now producing more milk than can be sold at the pegged price shows the influence of the pegged price upon the total production, and the fact that the peg has been lowered from \$3.39 per cwt. in 1929 to \$1.52 shows that the League has recognized the law of supply and demand to be still dominating the situation. Obviously the pegged price for a portion of the milk supply has been a factor in the action of the League members in increasing their production. Of course, they know that this increase of production is lowering their average price upon all sales, but the individual member considers it to his advantage to go on getting as much milk from his own herd as possible, either by adding to the herd or improving it.

It should be added that the decline in prices of dairy products seems to have been due in less degree to an increase of production than to a decline in the purchasing power of consumers. This does not affect the validity of the above analysis, for price is affected by the relationship between supply and demand whether changes occur on one side of the equation or the other.

It is apparent that the farmers who have these fluid milk contracts are faring much better than the great body of dairy farmers over the country, who must sell their milk only for manufacture into the other products. Furthermore, in considering the general loss of purchasing power which has befallen the farming population it must be borne in mind that even the low-priced dairy products are still more remunerative—especially to farmers who have built up herds of high productivity—than the common field crops or other primary products which can be marketed in abundance from almost a state of nature. Here is light on the world-wide disruption of trade relationships between primary and finished products.

Rising Costs of Distribution

The changes that have occurred in the buying and selling price of milk for household use, and in important items entering into the cost of distribution are shown in the chart below which gives the percentage change between the 1913 average and December, 1932.



Percentage Change, 1913 to December, 1932 in Cost, Distributing Expenses and Retail Selling Price of Fluid Milk in the New York Market.

A—Paid farmer by fluid milk distributor.
B—Railroad freight charges.
C—Delivery routemen's earnings.
D—Total spread for distribution.
E—Retail selling price, delivered.

The lesson of these charts and of this milk article is in the changed relations since 1913 between prices received by farmers, prices paid by consumers and the costs of transportation and distribution. On milk for the retail trade farmers receive 3 per cent more, but on all other milk substantially less, while consumers at retail pay 22 per cent more, railroad freight charges are 42 per cent higher, (railroad wages being 140 per cent higher) delivery route men receive 110 per cent more, and the total spread between producer and consumer on retail milk is 32 per cent higher.

As previously stated, the price paid to the farmer by distributors of fluid milk, although now down from \$3.39 per cwt. in 1929, is up from \$1.47 per cwt. in 1913 to \$1.52, or by 3 per cent, but the net price for all milk received by members of the League Cooperative Association has declined from \$1.47 to \$1.18 or by 20 per cent, as a result of the sliding scale of payments introduced in 1921 and the increasing surplus produced during more recent years.

Since 1913 practically every important item in the costs of distribution has been increased, despite improvements in operating efficiency and the investment of large amounts of new capital in the industry. Obviously the distributing companies would desire to keep costs as low as possible, but their costs, whether directly for wages or for supplies, nearly all in the end represent pay for personal services, and have shared in the general increase of such pay. Taxes are an item of no small importance to which this statement also applies.

Railroad freight rates, from the 201-210 mile zone, which is representative, have been increased from 32 cents per 10-gallon can to 45.5 cents, or by 42 per cent, which we have here-

tofore seen is in labor costs. The country station handling expense, cost of trucking from terminals, of pasteurizing and of bottling, nearly all of which represent labor cost directly or indirectly, have increased in harmony with the general wage movement, while the average earnings (including commissions and various allowances) of the routemen who deliver milk for the larger distributors have been increased from approximately $19 per week to $48 and since reduced to $40, leaving a net increase of 110 per cent, accompanied by an increase in the volume per route unit, while the workers have also benefited by the introduction of the six-day week, vacations with pay, group insurance, etc.

In view of the increase of distribution costs the advance in retail milk prices from 9 to 11 cents, or by 22 per cent, does not seem excessive, and according to the distributors has been made possible only by new economies, which they are continually striving to accomplish, and by the constant investment of new capital. The general rise of wages and all costs has necessitated large additions to capital to handle the business.

Price Fluctuations

During the period of inflation in 1916-1920, the increase in prices charged consumers, if calculated on a percentage basis, lagged behind the increase in prices paid to farmers, the difference being absorbed by the distributing companies, as may be seen from the following table:

Fluid Milk Prices, 1913-1920
(In cents per quart)

	1913	1917	1918	1919	1920
Paid to New York State Farmers					
Price, per qt..	3.26c	5.58c	6.96c	7.53c	7.52c
Increase over 1913, per qt.	—	+ 2.32c	+ 3.70c	+ 4.27c	+ 4.26c
% Increase over 1913....	—	+ 71%	+ 113%	+ 131%	+ 130%
Retail Price, New York City					
Price, per qt.	9c	12c	14c	17c	17c
Increase over 1913, per qt.	—	+ 3c	+ 5c	+ 8c	+ 8c
Increase over 1913 (%)....	—	+ 33%	+ 56%	+ 89%	+ 89%

When retail prices were reduced from 16 cents per quart in 1929 to the present 11 cents, the equivalent prices paid to the farmers was reduced from 7.29 cents per quart to 3.27, or by 4.02 cents, the remaining 0.98 cents being absorbed by the distributing companies in their operating expenses and net profits.

Keen competition exists in the business, because of the large number of independent distributors and the ease with which anyone may enter the business in a small way. One of the outstanding organizations in the industry is the Borden Company, which was originally established in 1857 and has made public its annual reports to shareholders since 1919. During the relatively prosperous thirteen-year period ended December 31, 1931, the company's sales aggregated more than $2,164,000,000, including all the company's sales of milk and other dairy products throughout the United States and Canada, on which the net profits available for dividends or for reinvestment to meet the demand for additional capital ranged from 2.32 to 5.93 per cent, and averaged 5.10 per cent on sales. This was the share of the value of this product, as paid for by consumers, that went to the capital employed in distribution over the thirteen years; the other 94.9 per cent was divided between the producers and the other factors in distribution, chiefly labor. No earnings figures for the industry as a whole are available, but the limited number of statements that are published show a uniformly narrow margin of profit, with some concerns reporting deficits.

An investigation into the milk industry is being conducted at the present time by a joint committee of the New York State Legislative and is expected to provide detailed information regarding the various items in cost of distribution which should be very useful in studying the industry.

Sanitary Regulations

It must be recognized that part of the increase in cost during the years since 1913 is directly due to higher standards demanded in milk handling and inspection for the protection of the public health. The required pasteurization of all milk is an example and the Board of Health of New York City only recently has announced an amendment to the Sanitary Code which prohibits after June 1, 1933, the sale of milk in any containers other than bottles or other individual containers, filled and properly labeled at the plant where pasteurized, except that under certain restrictions loose milk will be permitted to be sold to restaurants for cooking, to hospitals, etc. This action was taken after a report by an independent investigating commission had found definite health hazards in milk as sold over the counter. It will mean, however, a further increase in the expense of distribution and will require an expenditure for remodeling plants and equipment estimated at several million dollars.

Regardless of possible changes in retail prices and costs of distribution, however, there would appear to be small promise of any material improvement in prices received by the farmers for all milk if the current heavy production is continued and the surplus sold for whatever it will bring for use in manufacturing. To date there has been little evidence of curtailment in production by the dairy farmers, the reason probably being that milk, even at present prices, is still the most profitable cash crop in this section.

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